

PROMOTING ECONOMIC OPPORTUNITY AND OWNERSHIP

Supported by the pro-growth policies President Bush and the Congress adopted during his first term, the U.S. economy is strong and its fundamentals point to continuing prosperity and expansion. The economy is creating new jobs; the unemployment rate is lower than the average of the 1970s, 1980s, and 1990s; previously discouraged workers are re-entering the workforce and American businesses are investing for the future in new equipment and technology.

The economy's expansion has been steady and broad-based, with new investment and job growth in virtually all major industries, and across all regions of the country. There are several aspects of this expansion that merit special attention, including: the current features of our expansion that suggest long-term economic health; the policies that restored growth to the economy; and the economic policies needed to keep our economy on a healthy economic path.



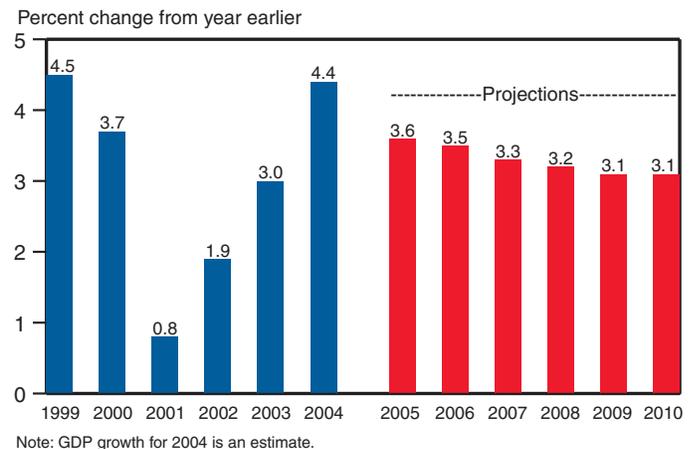
President George W. Bush participates in a conversation about homeownership at the Carpenters Training Center in Phoenix, Arizona, March 26, 2004.

The Economy's Current Condition

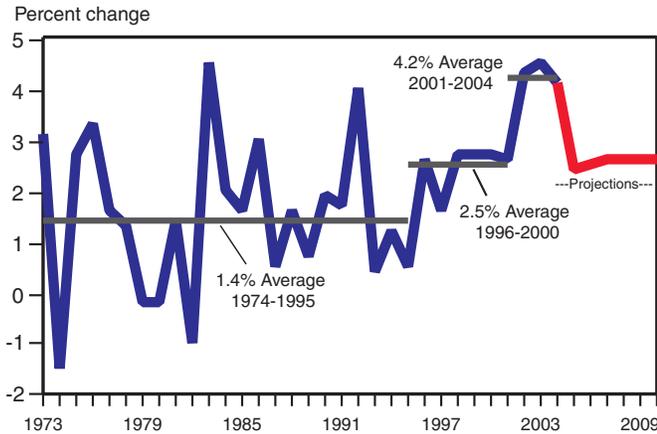
As of the fourth quarter of 2004 the economy had grown 13 straight quarters, and production and income had grown more than 10 percent. The economy generated over 2.6 million new jobs from August 2003 through December 2004, the unemployment rate fell by almost a full percentage point, and a wide range of indicators point to continued strong economic growth and improving labor markets in 2005.

The Administration is forecasting 3.6 percent real GDP growth in 2005 and 3.5 percent growth in 2006, which approximates the consensus of private-sector forecasters. A wide range of indicators support this forecast.

Strong Sustained Real GDP Growth



Strong Productivity Growth

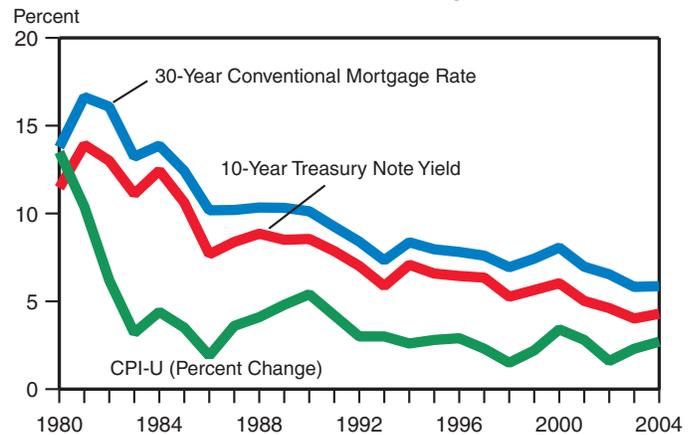


Note: Productivity growth for 2004 is an estimate.
 Strong productivity growth means more competitive companies and higher paid workers.

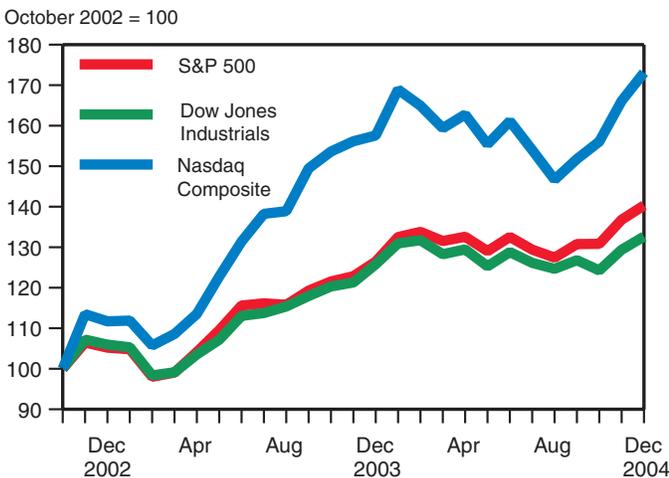
For example, labor productivity rose at an average rate of 2.5 percent from the beginning of 1996 to the end of 2000, significantly faster than productivity growth over the previous 20 years. Since the business cycle peak in the first quarter of 2001, productivity has risen even faster, at a robust 4.2 percent average annual rate. Productivity growth has, as expected, slowed somewhat in 2004, but at 3.1 percent growth over the past 12 months it continues to grow at historically high levels that help restrain price pressures, increase the standard of living, and sustain economic momentum.

Price stability is also an important factor for strong growth in the economy. Even with a recent spike in energy prices, overall inflation remains subdued, helping to sustain business and consumer confidence in the economy. Historically low interest rates, in part made possible by low inflation, also create a positive environment for growth by helping individuals make large-scale purchases, such as homes, or to refinance old loans at lower cost. Low interest rates have also allowed businesses to achieve substantial interest cost savings, strengthen their balance sheets for the future, and take better advantage of new investment opportunities.

Low Interest Rates and Low Inflation Have Helped Restore Strong Growth



Major Stock Indexes



The news on labor markets, output, productivity, inflation, and interest rates all suggest the economy has moved to a higher plane of long-term, sustainable expansion. This good news is reflected in the performance of the equity markets: stock prices rose sharply in 2003, and again in the closing months of 2004. All the major stock indices are at or near their highest levels since September 11, 2001. Increases in equity markets have added \$4 trillion to household wealth since September 2002, restoring much of the losses that followed the stock market decline of 2000-2002. Combined with gains in housing prices, household net worth has risen \$8.5 trillion since the third quarter of 2001.

Data released in the final days of 2004 and in early 2005 reinforce expectations for continued economic strength. Industrial production, which started to slide in mid-2000, began to recover again by the end of 2001 and reached a new high in December of 2004. Oil prices have fallen from their highs. And business optimism, as measured by a periodic survey released by the National Federation of Independent Business, reached a 20-year high in December, driven especially by business plans for new hiring.

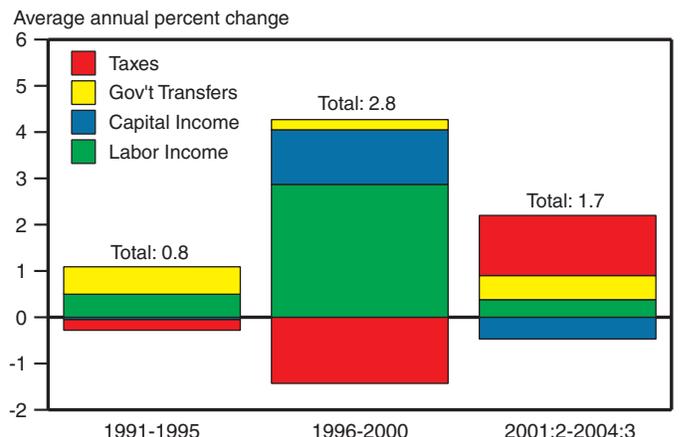
Tax Relief: Why it Worked

The recent economic performance is remarkable considering that the U.S. economy was in a recession by early 2001, faced a major national emergency in September 2001, and endured the revelation of major corporate scandals and two wars. Yet the recession of 2001 was relatively short-lived and shallow, and it gave way to a robust expansion largely because the Congress responded to the President's call and enacted tax relief in 2001, 2002, and 2003.

Lower tax rates enacted in 2001 reduced obstacles to growth by increasing the incentives to work, save, invest, innovate, and start new businesses. In 2002, the President worked with the Congress to improve investment incentives, which reversed a two-year downward trend in business investment; as of the fourth quarter of 2004, business investment had increased seven consecutive quarters.

In 2003, the President worked with the Congress to accelerate the 2001 tax relief. Also in 2002, an improvement in the tax treatment of small business investment helped many entrepreneurs put more of their capital to work in growing their firms. And the President won significant reductions in the tax rate on dividends and capital gains. This added tax relief reduced distortions arising out of the tax code that unfairly and unwisely subjected some forms of investment income to excessively high tax rates, and fundamentally improved the investment and saving climate in the United States. Lower dividend and capital gains tax rates also significantly reduced the incentives that previously drove businesses to rely unduly on debt financing.

Contributions to Growth in Real Per Capita Disposable Income



Taxes went from being an extra drag on the economy in the 1990s to becoming a powerful stimulus through the President's program.

POLICIES FOR A STRONGER ECONOMY

The economy has rebounded from its period of weakness, and even with a recent spike in energy prices and continued weak economic growth among our trading partners, it appears poised for continued strength. An extended economic expansion is far from assured; however, the Administration will continue to advance policies that promote growth, opportunity, and ownership. These steps will help America remain the world's best place to do business and create jobs.

Tax Policy

As outlined above, tax relief was a primary reason for the economy's rebound. In 2004, the President signed into law the fourth tax cut in as many years to maintain that tax relief, including

the new 10-percent tax bracket, the marriage penalty relief, the increase in the child tax credit, dividend tax relief, and other provisions that will continue at their current levels in most cases through 2010. The President has called on the Congress to make this tax relief permanent so that families and businesses can invest and plan with confidence.

Even with all the positive changes the President has signed into law, the Federal income tax code still discourages economic growth in many ways. For example, the income tax continues to discourage saving for many taxpayers, and so the President has proposed Retirement Savings Accounts, which would replace the complex array of retirement saving incentives currently in the tax code, such as IRAs, Roth IRAs, and similar saving vehicles. The President has also proposed Employer Retirement Savings Accounts to simplify the saving opportunities individuals have through their employers.

The President also proposed Lifetime Savings Accounts that would, for the first time, allow individuals to save on a tax-preferred basis for any purpose. While important to all Americans, Lifetime Savings Accounts are especially important to low-income individuals and families who need to save, but cannot afford to lock up funds for retirement that may be needed for an emergency in the near-term. The President also proposed Individual Development Accounts that would give extra financial incentive to certain low-income families to set aside funds for major purchases, such as a first home.

For generations, the tax code has encouraged Americans to spend first and save second. These proposals would level the incentives to save and consume, thereby promoting a culture of saving in America that is essential to future prosperity.

These saving proposals would help address one of the tax code's many flaws, but they cannot address all the problems the tax code presents for the economy. Therefore, the President has called for a fundamental reform of the Federal income tax system to make it simpler, fairer, and more pro-growth. The Federal income tax code is not just a complicated mess; it is also a maze of special-interest loopholes that cause America's taxpayers to spend more than six billion hours every year on paperwork. Work, entrepreneurship, investment, ownership, and even education are discouraged by our tax system. Businesses routinely make decisions about the deployment of capital not on economic merits alone, but also on the relevance of certain chapters of our tax code.

The President appointed a bipartisan Advisory Panel on Fundamental Tax Reform to report to the Secretary of the Treasury by July 31, 2005, on options to reform the tax code. These options will form the basis of efforts to enact reforms that meet the President's objectives of simplification, fairness, and a more pro-growth tax system, while recognizing the importance of homeownership and charity to American society.

Litigation Reform

The costs of litigation per person in the United States are far higher than in any other major industrialized nation in the world. Lawsuit costs have risen substantially over the past several decades, and a significant part of the costs go to paying lawyers' fees and transaction costs—not to compensating the injured parties. The litigation explosion is clogging our civil courts and threatening jobs across America. Businesses with \$10 million or more in revenue bear an average annual cost of \$150,000 from litigation. Small businesses with less than \$10 million in revenue bear 68 percent of business tort liability costs, even though they only take in 25 percent of business revenue.

The President is pushing the Congress to pass legislation that reduces the burden of frivolous lawsuits on our economy. The President supports enactment of medical liability reform, class action lawsuit reforms, and asbestos litigation reform to expedite fair resolutions and curb the costs of lawsuits for all Americans.

Frivolous lawsuits and excessive jury awards are driving many health care providers out of communities and forcing doctors to practice defensive medicine. This reduces access to medically necessary services and raises the costs of health care for all. The President has proposed proven reforms, such as common-sense limits on non-economic damages, to make the medical liability system more fair, predictable, and timely.

The President's proposed class action reforms seek to limit the abuse of large, nationwide class action cases and provide justice to the truly injured parties. Class actions are an important and intrinsic part of the U.S. legal system. However, class actions are heavily abused, which in turn harms affected parties and undermines the American judicial system. In particular, injured parties often receive awards of little or no value while lawyers receive large fees. The proposed class action reform legislation recognizes that large interstate class actions require Federal court jurisdiction because they typically affect more citizens, involve more money, and raise more interstate commerce issues than any other type of lawsuit. In addition, the President wants to end the practice of "judge shopping," where trial lawyers file cases only in jurisdictions likely to favor plaintiffs. These reforms do not alter the right of a plaintiff to bring a legitimate claim, or change controlling substantive law, but provide additional protection and information to class members.

Asbestos cases have generated the longest-running mass tort litigation in U.S. history and have led to the bankruptcies of at least 74 companies and to more than 50,000 lost jobs. Within the past few years, there have been sharp increases in the number of asbestos claims filed annually. The current system is costly to administer, with total projected costs estimated at between \$200 and \$265 billion. These costs have driven exposed defendants into bankruptcy and may leave little or no funds to pay future asbestos victims. The President has stressed the need for reform and urged the Congress to find a fair and permanent solution.

Regulatory Reform

Excessive regulations can prevent the creation and growth of new small businesses and the jobs they create; in the first term, the Administration slowed the growth of new rules by 75 percent. The President wants to streamline regulations further and reduce paperwork to alleviate the burdens that unduly handicap America's entrepreneurs and job creators. The Administration is taking action in several areas to streamline Federal regulations, while still moving forward with crucial safeguards for homeland security, human health, investor and environmental protection. Regulations should be analyzed based not just on their benefits, but also on their costs. When regulations are proposed, the scientific research supporting their enactment must be sound, and subject to careful scrutiny. And when regulations are out of date, they must be reviewed for relevancy, and to make sure the benefits they produce are at least equal to their costs.

Health Care Costs

The rapid pace of health care inflation slows job growth, reduces the growth rate of worker wages, and makes health care less accessible and less affordable for consumers. When employers have to pay more for health coverage for their workers, they can afford less for worker paychecks. Ultimately, the increase in overall labor costs to U.S. employers, as a result of rising health care costs, damages our economy's global competitiveness.

Some employers, especially small businesses, struggle to provide even basic health insurance for their employees. State and national rules often prevent small businesses from banding together to purchase health coverage at the same rates paid by large companies. The President proposes to address this problem through Association Health Plans, which would permit cross-State health-purchasing alliances of small businesses and other organizations. In addition, the President

would make health care more affordable by offering tax credits for employer contributions to Health Savings Accounts. These accounts allow employees to save tax-free for their out-of-pocket health costs, and are paired with high-deductible insurance policies that cover hospitalization and other major health care costs.

Among the drivers for health care inflation are the out-of-control costs that come from unnecessary medical liability lawsuits. As mentioned previously, the President has an aggressive plan to reform our medical liability system. These reforms are critical because frivolous lawsuits have already chased many doctors out of the practice of medicine and make health care less accessible for millions of Americans. And for the doctors who remain, these lawsuits are an ever-present fear. Doctors wary of getting sued practice defensive medicine, ordering more laboratory tests or examinations than are medically necessary, which ultimately drives up health care costs for everyone. And because of the number of lawsuits—even those that are dismissed—insurers for doctors and hospitals raise premiums, and these higher costs of practicing medicine are passed on to consumers. Even if your doctor has never been sued, and even if you rarely visit the doctor, your health care has become far more expensive because of the abuse of our medical liability laws. Those States that have adopted common-sense reforms, such as caps on punitive damages and limits on non-economic damages, have seen smaller and more manageable increases in doctor's liability insurance premiums. The President intends to work with the Congress this year to adopt similar reforms nationally.

The President also supports investments in and accelerated deployment of health information technology that will further help to control rising health care costs. These technologies can reduce medical errors, improve patient care, and save doctors and nurses time, ultimately saving our health care system dollars.

Another way to control rising health care costs is by closing loopholes that slow the movement of more affordable generic drugs to the marketplace. The Administration has taken action to improve access to generic drugs by: limiting the time a drug company can delay the marketing of a generic competitor; instituting rule changes to prevent drug companies from blocking the marketing of generic versions by using patents on minor features; and tightening the rules on patent applications so that false statements to get a patent result in criminal charges. These actions are bringing generic drugs to the market more quickly, and will save American consumers \$35 billion over 10 years—savings that go not only to the consumers, but also to Medicare and Medicaid programs administered by the States.

Trade

President Bush's top economic priority is the creation of more jobs for American workers. Free and fair trade helps create more higher-paying jobs for American workers by opening new markets for American products and services, expanding choices for American consumers, and attracting foreign companies to invest and hire in the United States. America is economically stronger when we participate fully in the worldwide economy because 95 percent of the potential customers for American products live outside the United States.

Trade agreements like the North American Free Trade Agreement and the World Trade Organization (WTO) have generated benefits—lower prices and more choices—totaling \$1,300 to \$2,000 annually for the typical U.S. family. Lowering barriers to trade by even one-third will boost the world economy by as much as \$613 billion—and the U.S. economy by \$144 billion a year. To the typical family of four, that means an additional \$2,000 or more a year in savings.

Exports have reached record levels during the Bush Presidency. President Bush, working closely with the Congress, won Trade Promotion Authority to enable quicker passage of trade agreements. This was the first time the Congress approved Trade Promotion Authority in eight years. Using this

authority, the Bush Administration has completed free trade agreements with 12 countries, including Australia, Morocco, Bahrain, Chile, Singapore, and Jordan, and is negotiating free trade agreements with 10 others. In addition, the Administration is in the process of forming a Free Trade Area of the Americas, which will become the world's largest free trade area.

The Administration also played a critical leadership role in successfully launching a new round of global trade negotiations at the WTO, and has developed an aggressive plan to open international markets for U.S. farmers—which helped generate a 10-percent increase in agricultural exports between 2000 and 2003.

The President recognizes that some communities and some industries face adjustments in the global economy. That is why he signed a major expansion of assistance to help workers acquire new skills and find new jobs. The Trade Act of 2002 nearly tripled the Trade Adjustment Assistance program. In 2003 it provided some \$1.3 billion in training and income support, with nearly 200,000 workers eligible for assistance. President Bush is ensuring that U.S. trading partners abide by their international commitments by aggressively enforcing U.S. trade laws. For example, the Administration brought the first-ever WTO case against China for its discriminatory tax treatment against U.S. semiconductor makers. In July 2004, China agreed to end this unfair practice.

Energy

It is critical to our economy to have affordable, reliable, and secure energy supplies. President Bush in his first term put forward the first comprehensive, long-term energy policy in a decade to meet this goal through conservation, investment in new technology, and development of new domestic sources of energy. The Bush Administration has completed, or is in the process of implementing, nearly 75 percent of the 106 recommendations contained in the President's comprehensive National Energy Policy, such as filling the Strategic Petroleum Reserve to capacity.

President Bush also proposed modernizing the electricity grid by reforming outdated laws, opening access to the transmission grid, establishing regional planning and coordination, and establishing mandatory reliability standards to prevent blackouts. The President has advocated funding for clean coal research, including FutureGen, and increasing use of clean coal technology; funding for nuclear energy research and development; new efficiency standards for consumer products; tax incentives for use of renewable sources of energy like wind and solar power; and the opening of a small area (less than one percent) of the Arctic National Wildlife Refuge for environmentally responsible oil and gas exploration. The Arctic National Wildlife Refuge has the potential to provide over one million barrels of oil a day and provides access to one of the largest known reserves of natural gas in the United States.

President Bush launched a groundbreaking initiative to develop technologies and infrastructure to produce, store, and distribute hydrogen for use in fuel-cell vehicles, electricity generation, and other applications. Hydrogen-powered fuel cells hold the potential to power cars, trucks, homes, and businesses while producing virtually no pollution or greenhouse gases.



A hydrogen refueling station at Los Angeles International Airport.

Innovation and Ownership

In virtually every industry, American companies and entrepreneurs are exercising the power of innovation to meet 21st Century challenges. Invention, commercialization, and diffusion of new ideas into new products and services directly affect the pace of productivity growth and the quality of peoples' lives. Innovation lowers costs to consumers and brings new products to the market.

The greatest incentive for innovation is a healthy economy that rewards the inventor and investor. The Administration supports strong protection of patent rights and research and development, as well as the enforcement of anti-trust laws so that new competition is always welcomed. The President has laid the foundation for healthy innovation with tax relief that rewards those who create jobs and invest capital in new ideas. He has also proposed many other policies to build on this base:



President Bush talks with an employee at U.S.A. Industries in Bay Shore, N.Y., March 11, 2004.

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- The President has proposed to make the Research and Experiment tax credit permanent to encourage technological discovery.
- The President proposes to increase Federal spending on new research and development to \$132 billion, an increase of one percent over 2005 and an all-time high.
- He has established programs to accelerate the adoption of hydrogen fuel technology, a new and promising energy source, which has the potential to reduce our dependence on foreign sources of energy.
- His proposals would transform health care through the rapid application of new health information technology, thereby reducing medical errors and health care costs.
- The President has called for universal, affordable access for broadband technology by the year 2007.
- The President has placed a priority on nanotechnology, information technology, and scientific and technological standards.

As our economy continues to expand, the Federal Government will help communities respond to and prepare for changing conditions, particularly as some industries restructure and new industries appear. To help workers in poor communities, the President is proposing Opportunity Zones and other initiatives to provide tax relief, and attract new business, and improve housing and job training. In addition, he has signed legislation and increased funding to support the cleanup of former industrial sites, which are known as brownfields.

A key element of the Administration's policy is to promote ownership in America. The Administration has promoted and will continue to support policies that allow individuals to take greater control over their lives through private ownership. When families have assets, they have a foundation of stability to help them through difficult periods. A family that saves, owns a home, or invests through a retirement, health, or education fund is building toward a brighter future and contributing to our economy's long-term economic health.

The best place to see these effects is where people live. More Americans own their own homes than ever before, and the value of those homes is rising at a steady pace. Our strong housing market is

a testament to the faith that Americans place in their homes as a long-term investment. The President has placed a high priority on promoting further gains in homeownership, particularly among minorities. Already, minority homeownership is at a record high, and in 2002 the President set an ambitious goal to add 5.5 million minority homeowners through 2010. Through downpayment assistance programs, financial literacy efforts, tax incentives for building affordable homes, and Individual Development Accounts, the President is promoting the kinds of policies that will strengthen our neighborhoods and communities and provide more Americans a chance to call something their own.

The same principle applies to other Presidential policies. Health Savings Accounts provide a better way for Americans to control and spend their health care dollars. Lifetime Savings Accounts will provide a better way for Americans to save for college tuition and other goals. Personal Retirement Accounts under Social Security will provide a better way for Americans to save for their own retirement, using a portion of their payroll taxes. In all these proposals, personal ownership is the common feature, because it is the best way to achieve financial independence and prosperity.

During the past four years, this Nation experienced significant economic challenges that tested the resolve of the American people. But as is now clear, that resolve was never in question. The economic recovery has now become a strong expansion that is bringing prosperity to more communities across America. Yet the on-going weakness in other nations' economies serve as a reminder that the United States cannot afford to take a strong economy for granted. Effective tax, monetary, labor, regulatory, environmental, education, trade, and national security policies are all necessary for a strong and growing economy.

At the same time, all these policies merely complement the effort, ingenuity, and strength of individual workers and companies that comprise our \$12 trillion economy. Through the pursuit of pro-growth policies, our economy is once again growing at a strong and sustainable pace. Through a growing economy, Federal receipts are once again rising at a steady rate. Combined with spending restraint, rising revenues will reduce the near-term budget deficit. By addressing the near-term deficit and the long-term imbalances in entitlement programs, America will further reinforce our prospects for a strong economy in the years ahead.